

On Tuesday, February 4th, Standard & Poor's downgraded Puerto Rico's general obligation bonds and related debt to BB+, making it the first rating agency to bring the Commonwealth's debt rating to below investment grade. General Obligation bonds, the Highway and Transportation Authority, and other Commonwealth-guaranteed debt were downgraded one notch from BBB-. The Government Development Bank (GDB) and appropriation-backed debt were downgraded two notches to BB. All affected credits remain on Creditwatch negative. Puerto Rico's Electric and Power Authority, Aqueduct and Sewer Authority, and Sales Tax Corporation (COFINA) ratings were not included in the downgrade. Appleton Partners, Inc. does not have any exposure to Puerto Rico or related debt in client accounts. We previously held the Senior Lien Sales Tax Corporation Bonds (COFINA), but exited the investment in late 2013.

The main driver of the rating action was S&P's concerns regarding the Commonwealth's liquidity, even in the event of a potential debt issuance at the end of February. The Commonwealth frequently relies on external liquidity to roll-over short-term debt and finance operating deficits. S&P believes this reliance is not commensurate with an investment grade rating.

Moody's (Baa3) and Fitch (BBB-) have also warned Puerto Rico of a potential downgrade, focusing on the Commonwealth's ability to successfully access the capital markets for long-term financing. The Commonwealth expects to issue a sizable bond deal near the end of February. S&P has noted that if the deal is brought to market successfully, it could remove the Creditwatch negative designation.

At this point we do not expect a broad wave of selling pressure, as a downgrade was largely expected by the market. Most mutual funds include prospectus language that allows for flexibility in the event of a downgrade or includes language that states downgrades will not result in forced selling of securities. Trading activity in Puerto Rico bonds may accelerate post-downgrade, but at this time we do not believe the idiosyncratic events of the Commonwealth will have an effect on the broad municipal market.

| Issuer | Moody's | S&P | Fitch | Watch Negative? | Outlook Neg | Outlook Stable |
|------------------------|---------|-----|-------|-----------------|-------------|----------------|
| GO | Baa3 | BB+ | BBB- | M/S/F | | |
| GDB | Baa3 | BB | N/A | M/S | | |
| Retirement System | Baa3 | BB | BBB- | M/S/F | | |
| Highway Revenue | Baa2 | BB+ | N/A | M/S | | |
| Transportation Revenue | Baa3 | BB+ | N/A | M/S | | |
| PREPA | Baa3 | BBB | BBB- | M | S | F |
| PRASA | Ba1 | BB+ | BBB- | M/S | F | |
| COFINA Sr | A2 | AA- | AA- | M | S | F |
| COFINA Sub | A3 | A+ | A+ | M | S | F |
| UPR | Ba1 | BB+ | N/A | M/S | | |

Source: Bloomberg, Moody's, S&P, Fitch

***BASED ON LONG-TERM AND CONTINUING WEAK ECONOMIC CONDITIONS,
CONCERNS ABOUT LIQUIDITY AND MARKET ACCESS, AND THE
COMMONWEALTH'S EXPOSURE TO EXTERNAL RISKS, PUERTO RICO DOES NOT
AT THIS TIME FIT APPLETON PARTNERS' HIGH-GRADE INVESTMENT STRATEGY***

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